

Indiana Department of State Revenue

Revenue Ruling #2005-11ST

August 11, 2005

Notice: Under IC 4-22-7-7, this document is required to be published in the Indiana Register and is effective on its date of publication. It shall remain in effect until the date it is superseded or deleted by publication of a new document in the Indiana Register. The publication of this document will provide the general public with information about the Department's official position concerning a specific issue.

ISSUES

Sales Tax—Environmental Control Equipment

Authority: IC 6-2.5-2-1; IC 6-2.5-5-3; 45 IAC 2.2-5-8(g) and (j).

STATEMENT OF FACTS

The taxpayer manufactures stainless steel and plastic surgical instruments and accessories. All of the taxpayer's sales are to original equipment manufacturers for resale; the taxpayer has no sales which are subject to Indiana sales tax. All operations—including manufacturing, fabrication, assembly, product engineering, and administration—take place at the taxpayer's Indiana location.

Taxpayer intends to purchase and install an environmental control system. The taxpayer states that the environmental control system is required to satisfy the medical industry's high standards for quality and product cleanliness; if the quality standards are not met, the products will be rejected by the taxpayer's customers and will be ultimately scrapped.

Taxpayer states that the machinery within the plant operates at extremely accurate and precise measurements; however, the accuracy and precision is diminished by humidity and temperature variations within the plant. As well, the steel and plastic materials used in the manufacturing can be affected by the temperatures within the plant and by the plant cleanliness. The environmental control system will ensure that the raw materials remain within tolerance through all phases of production and also will prevent dust and other particles from contaminating the final product.

The taxpayer seeks a ruling as to whether the environmental control system meets the criteria to qualify for the manufacturing exemption from sales tax.

DISCUSSION

IC 6-2.5-2-1 imposes sales tax on all retail transactions made within Indiana. IC 6-2.5-5 names the transactions that are exempt from sales tax. IC 6-2.5-5-3 exempts from sales tax the purchase

of manufacturing machinery, tools, and equipment if the person acquiring that property acquires it for direct use in the direct production, manufacture, fabrication, assembly, extraction, mining, processing, refining, or finishing of other tangible personal property. The taxpayer does produce tangible personal property. The question is whether the environmental control system is directly used in the direct production of tangible personal property.

The determination of exempt use is fact sensitive. 45 IAC 2.2-5-8(g) interprets IC 6-2.5-5-3. The regulation discusses equipment having an immediate effect upon the article being produced. It states:

Machinery, tools, and equipment which are used during the production process and which have an immediate effect upon the article being produced are exempt from tax. Component parts of a unit of machinery or equipment, which unit has an immediate effect on the article being produced, are exempt if such components are an integral part of such manufacturing unit. The fact that particular property may be considered essential to the conduct of the business of manufacturing because its use is required either by law or by practical necessity does not itself mean that the property "has an immediate effect upon the article being produced." Instead, in addition to being essential for one of the above reasons, the property must also be an integral part of an integrated process which produces tangible personal property.

The environmental control system may be considered to be essential, but it needs to be an integrated part of an integrated process. The equipment does maintain a controlled environment to facilitate the manufacturing process, but the controlled environment is a general environment, not an environment restricted and integrated only to the manufacturing process. Additional support that the environmental control system does not qualify for exempt status is the fact that the prior system appears to have been adequate for production.

45 IAC 2.2-5-8(j) states that ventilation and cooling equipment for general temperature control is taxable. The environmental control system affects all stages of production, from pre-production, production, and post-production. Its effect is not upon the production phase alone but also upon storage before and after production. For this reason, it is general ventilation and cooling equipment, not production equipment.

RULING

The Department rules that the environmental control system does not qualify for a sales tax exemption under IC 6-2.5-2-1.

CAVEAT

This ruling is issued to the taxpayer requesting it on the assumption that the taxpayer's facts and circumstances, as stated herein are correct. If the facts and circumstances given are not correct, or if they change, then the taxpayer requesting this ruling may not rely on it. However, other taxpayers with substantially identical factual situations may rely on this ruling for informational purposes in preparing returns and making tax decisions. If a taxpayer relies on this ruling and the Department discovers, upon examination, that the fact situation of the taxpayer is different in any material respect from the facts and circumstances given in this ruling, then the ruling will not

afford taxpayer any protection. It should be noted that subsequent to the publication of this ruling, a change in statute, regulation, or case law could void the ruling. If this occurs, the ruling will not afford the taxpayer any protection

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